IN THE

Supreme Court of the United States

SEP 16 1944
CHARLES ELMORE CROPLEY
CLERK

OCTOBER TERM, 1944.

No. 475

THE PENFIELD COMPANY OF CALIFORNIA,

Petitioners,

vs.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

Petition for Writ of Certiorari to the Ninth Circuit Court of Appeals and Brief in Support Thereof.

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To the Honorable Chief Justice and to the Associate Justices of the Supreme Court of the United States:

Your petitioner, The Penfield Corporation of California, hereby prays that a writ of certiorari may be granted directing the Circuit Court of Appeal of the United States for the Ninth Circuit to certify to this Court, for review and determination, the case of The Penfield Company of California, a corporation, appellant, vs. the Securities and Exchange Commission, appellee, being cause No. 10487 in the United States Circuit Court of Appeals for the Ninth Circuit.

A.

Jurisdictional Statement.

Jurisdiction is conferred by Section 22(b) of the Securities Act of 1933, 15 U. S. C. 77v (b) and by Securities and Exchange Act, Title 15, Section 77v (a) and Title 28, Sections 225 and 347, U. S. Codes. See also *Cobbledick v. United States,* 309 U. S. 323, 330, 84 L. Ed. 783, 787.

The decision of the Circuit Court of Appeals was rendered June 30, 1944, by a majority of the court; a concurring opinion was filed by Judge Mathews July 19, 1944; a petition for rehearing was duly filed on July 25, 1944, and denied August 8, 1944 [R. 360-361].

B.

Questions Presented by This Appeal.

1. Is the Securities and Exchange Commission authorized to delegate its power of issuing subpoenas *duces tecum* to one of its investigators and to give that investigator authority to require the production of any books, papers, correspondence, memoranda, or other records, or must the Securities and Exchange Commission itself make a finding of "probable cause" and a finding that they deem the papers relevant or material to the inquiry?

2. Is such a delegated authority an unknown roving commission forbidden by the Fourth Amendment to the Constitution of the United States?

3. Is the act of Congress which gives the Securities and Exchange Commission authority to subpoena books, papers, correspondence, memoranda, or other records, a violation of Article III of the constitution of the United States which gives judicial functions only to the courts?

4. Are contracts for the bottling of whiskey (which must be done under an alcohol tax unit permit) securities within the meaning of Section 2(1) of the Securities Act of 1933 as amended?

5. Does the Securities and Exchange Commission have jurisdiction over dealings in alcohol bottling where that subject matter comes under the alcohol tax act?

C.
The Importance of the Questions Involved.

It is important that this honorable court grant certiorari because of the importance of the questions involved which have heretofore not been passed upon by this honorable court. There has been no construction of the Securities and Exchange Commission covering the particular sections here challenged except by the Ninth Circuit Court of Appeals and this is the first case which raises the particular issues here presented.

D.
Statutes Involved.

The statutes involved are Section 19(b) of the Securities Act of 1933 as amended and supplemented by Section 22 (b) of the said Act; Section 2 (1) of the Securities Act as amended in 1933; the Fourth Amendment to the Constitution of the United States.

The Securities and Exchange Act of 1933, Section 19(b), provides as follows:

> "(b) For the purpose of all investigations which, *in the opinion of the Commission*, are necessary and proper for the enforcement of this title, any member of the Commissioner or any officer or officers desig-

nated by it are empowered to administer oaths and affirmations, subpoena witnesses, take evidence and require the production of any books, papers or other documents *which the Commission deems relevant or material to the inquiry.* Such attendance of witnesses and the production of such documentary evidence may be required from any place in the United States or any Territory at any designated place of hearing." (Emphasis added.)

Opinion of the Ninth Circuit Court of Appeals is contained in the transcript of the record [R. 344]:

E.
Statement of the Case.

The Securities and Exchange Commission instituted an investigation of The Penfield Company of California, a California corporation, to determine whether certain warehouse receipts and bottling contracts for the bottling of whiskey were being handled by The Penfield Company of California and also whether it had in any way transacted sales of stock through the mails.

The Securities and Exchange Commission made two orders as follows:

The order of the Securities and Exchange Commission alleged as follows:

"The Commission, having considered the aforesaid report by members of the staff, and for the purpose of (1) determining whether the persons named in the caption of this Order have violated or are about to violate the provisions of Section 5(a) and 17(a) of the Securities Act of 1933; and (2) aiding in the enforcement of said Acts; deems it necessary and

appropriate that an investigation be made to determine whether said persons have engaged in the acts and practices set forth in paragraph II hereof or any acts or practices of similar purport or object."

In a supplemental order of the Securities and Exchange Commission the Commission alleges as follows:

"The Commission, having considered the aforesaid report by members of its staff, and for the purpose of (1) determining whether the companies and persons named in the caption hereof have violated or are about to violate the provisions of Sections 5(a) and 17(a) of the Securities Act of 1933; and (2) aiding in the enforcement of said Act; deems it necessary and appropriate that an investigation be made to determine whether the said companies and persons, or any of them, have engaged in the acts and practices set forth in paragraph III hereof, or any acts or practices of similar purport.

"It Is Ordered, pursuant to Section 20(a) of the Securities Act of 1933 that the order and supplemental order directing an investigation mentioned in paragraph I hereof be and it hereby is supplemented and amended to include for determination the matters set forth in paragraph V hereof.

"It Is Further Ordered, pursuant to the provisions of Section 19(b) of the Securities Act of 1933 that for the purpose of such investigation, William Green, C. J. Odenweller, Jr., Charles E. Greaney, Hiram C. McDade and Harold O. Schroeder, and each of them, is hereby designated an officer of the Commission and empowered to administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of any books, papers, correspondence, memoranda or other records

deemed relevant or material to the inquiry, and to perform all other duties in connection therewith as authorized by law."

The Commission itself at no time made any order or finding as to what it deemed relevant or material to the inquiry as provided by Section 19(b) of the Securities and Exchange Act, nor did the Commission in any of its orders declare that "in the opinion of the Commission these things are necessary and proper for the enforcement of this title." Following these proceedings a subpoena *duces tecum* was issued [Exhibit "C"].

Subsequent to the issuance of these orders of the Commission a subpoena duces tecum was issued [Exhibit C, R. 15] directing A. W. Young, Secretary-Treasurer of The Penfield Company of California, *et al.*, 8900 West Beverly, Beverly Hills, Calif., to appear and produce twenty items set forth in the subpoena.

These items were:

1. Minute Book.
2. All stock certificate stub books and cancelled certificates of common and preferred stock.
3. Alphabetical list of stockholders and addresses (if not shown on stub books indicated in Item No. 2 above).
4. General Ledger.
5. Cash Book.
6. General journal.
7. Records reflecting the sale of whiskey and/or whiskey warehouse receipts by the corporation.

8. Records relating to the sale of bottling contracts of Bourbon Sales Corporation, Louisville, Kentucky, by the corporation.

9. Records relating to the sale of bottling contracts of The Penfield Company of California, by the corporation.

10. Correspondence files, including letters received from and copies of letters sent to, all stockholders of The Penfield Company of California.

11. Correspondence files containing letters received from, and copies of letters sent to, all persons to whom bottling contracts of Bourbon Sales connection with the sale of stock of The Penfield Company of California were sold.

12. All cancelled checks of the corporation.

13. Copies of confirmations or advices delivered in connections with the sale of stock of The Penfield Company of California or the sale of bottling contracts of Bourbon Sales Corporation, or The Penfield Company of California.

14. All original journal entries or journal vouchers supporting entries appearing in the general journal or cash books.

15. Copies of all prospectuses, sales material, sale letters, material in salesmen's kilts or similar documents used in connection with the solicitation and sale of stock in The Penfield Company of California.

16. Copies of all prospectuses, sales material, sales letters, material in salesman's kits or similar documents used in connection with the sale of bottling contracts of Bourbon Sales Corporation or The Penfield Company of California.

17. Purchase invoices or records supporting the acquisition of whiskey, whiskey warehouse receipts or bottling contracts by The Penfield Company of California from private individuals for cash or in exchange for stock, bottling contracts or other securities.

18. Purchase invoices or records supporting the acquisition of whiskey or whiskey warehouse receipts from distillers, whiskey warehouse receipts brokers or other persons or companies engaged in the whiskey business.

19. Sales invoices or records supporting the disposition of whiskey, whiskey warehouse receipts or bottling contracts procured from investors.

20. Employment or other records showing names of all employees, salesmen or other personnel with last known addresses.

Upon objections to their production the application was made to the District Court of the United States, which, after hearing, granted the order and stayed the execution of the appeal herein.

Grounds for Granting the Writ of Certiorari.

1. The District Court and Circuit Courts erred in holding that any investigator or employee of the Securities and Exchange Commission could himself issue a subpoena *duces tecum* and subpoena in all the books, papers, records, or other documents of a corporation, without the Commission itself making a finding that it deems them relevant and material.

If Congress had intended to have given the power of delegation to the Securities and Exchange Commission it would have been at no loss of words to say so, but the Congress, realizing the large number of corporations that could thus be subjected to a roving commission running riot, has strictly limited the power to subpoena books, papers and documents which the Commission deems relevant and material to the inquiry. The Fourth Amendment requires that before a search or a seizure can be made of books or papers that there be a finding of probable cause. There was none such in this case.

2. The District and Circuit Courts erred in holding that the Securities and Exchange Commission has any power to delegate of authority to issue subpoena *duces tecum*.

3. If it can be construed that the Securities and Exchange Commission can itself make an arbitrary finding as to what it deems *relevant and material*, such statute would itself be unconstitutional since the power to make that finding and the finding of reasonable and probable cause required by the Fourth Amendment can only be given to the courts under Article III of the Constitution.

4. The contract involved in these transactions and the transactions are not within the jurisdiction of the Securities and Exchange Commission as they are not within the term of investment contract defined by the Act.

5. Bottling contracts for whiskey are not contracts for a security, and therefore not within the scope of the Securities and Exchange Commission.

6. Where the contracts are matters relating to alcohol the scope of the Act is solely within the jurisdiction of the Alcohol Tax Unit.

7. The District Court erred in holding that each of the twenty items was within the scope and jurisdiction of the Securities Act giving the Commission power to investigate them and that the investigation was not far beyond the scope authorized by law.

Respectfuly submitted,

MORRIS LAVINE,

Attorney for the Penfield Company of California.

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BRIEF IN SUPPORT OF THE PETITION FOR WRIT OF CERTIORARI.

I.

The Securities and Exchange Act, Section 19(b), provides as follows:

> "(b) For the purpose of all investigations which *in the opinion of the Commission*, are necessary and proper for the enforcement of this title, any member of the Commission or any officer or officers designated by it are empowered to administer oaths and affirmations, subpena witnesses, take evidence, and *require the production of any books, papers, or other documents* WHICH THE COMMISSION DEEMS RELEVANT OR MATERIAL TO THE INQUIRY. Such attendance of witnesses and the production of such documentary evi-

dence may be required from any place in the United States or any Territory at any designated place of hearing." (Italics and caps ours.)

Section 19(b) of the Act empowers the Securities and Exchange Commission to invade the privacy of citizens and corporations by making of investigations which, in the opinion of the Commission, are necessary and proper for the enforcement of the Act. This section definitely gives the authority to issue subpoenas *duces tecum* after the Commission has made a finding that in its opinion the books, papers, documents and records are deemed by the Commission to be relevant or material to its inquiry.

It is admitted of course that the Commission made no such finding and that the attempt to issue a subpoena *duces tecum* was made by someone not even a member of the Commission.

The subpoena power is considered very drastic and no power to issue subpoenas exists except in accordance with the constitutional mandates.

Cudahy Packing Co. v. Holland, 315 U. S. 357, 86 L. Ed. 895;

Lowell Sun Co. v. Fleming, 120 Fed. (2d) 213, 86 L. Ed. 1191.

It will be noted that in order to secure a subpoena *duces tecum* from court such application for the subpoena must describe in the subpoena the papers, writings, books or other documents supposed to be in the possession or power of such witness, and it must be presented to a judge, who must be satisfied by the affidavit of the person applying, or otherwise, that there is reason to believe such papers,

writings, books or other documents are in the possession or power of the witness, and that the same, if produced, would be competent and material evidence for the party applying therefor.

It cannot be conceived that the Congress, in passing the Securities and Exchange Act, authorizing the issuance of a subpoena *duces tecum* in a proper case, intended that the subpoena *duces tecum* should be issued on any other conditions for the Commission than those provided for trial courts, and it did not give the Commission authority beyond or different than it gave to any person applying to a court for a subpoena *duces tecum*. Had it done any less than this it would have conflicted with the Fourth Amendment to the Constitution of the United States.

In *Grau v. United States*, 287 U. S. 124, 129, 77 L. Ed. 212, 214, the Supreme Court of the United States held that a warrant is void for failure to observe the statutory requirement that it state the particular grounds or probable cause for issuance, and for the further reason that it is based on affidavits which do not set forth the facts tending to establish the grounds of the application or probable cause for believing that they exist. The court held that the affidavits in that case were insufficient as they unduly narrowed the guaranties of the Fourth Amendment, in consonance with which the statute was passed. Those guaranties are thereby liberally construed to prevent impairment of the protection extended. (*Boyd v. United States*, 116 U. S. 616, 635, 29 L. Ed. 746, 751; *Gouled v. United States*, 255 U. S. 298, 65 L. Ed. 647, 650; *Go-Bart Imp. Co. v. United States*, 282 U. S. 344, 357, 75 L. Ed. 374, 382.)

As stated in the *Grau* case further, "Congress intended, in adopting Section 25 of Title 2 of the National Prohibition Act, to preserve, not to encroach upon, the citizen's right to be immune from unreasonable searches and seizures, and we should so construe the legislation as to effect that purpose."

Tested by the provisions of the Constitution and the statute before a valid subpoena *duces tecum* could be issued by the Securities and Exchange Commission it was necessary to be presented by the Commission a list of the things supposed to be in the possession or power of such witness, and thereupon it was necessary for the Commission to make a finding that, in its opinion, these books and papers were necessary for the proper enforcement of the title, and that the Commission deemed these articles relative or material to the inquiry.

No such request was made, apparently, of the Commission, and no finding was made by the Commission that it deemed these books and records necessary and proper for the enforcement of this title. [R. 2, 8, 12.]

At this point, for the sake of argument, if Congress could constitutionally delegate this judicial function to the Securities and Exchange Commission—to find what was necessary and proper for the enforcement of this title, then the Commission would have to have presented to it, in order to comport with the Fourth Amendment, an affidavit setting forth the articles sought and the reasons for seeking them. The documents and things sought would have to be described with particularity

The statutory provision either must be as broad as the constitutional guaranty which it seeks to avoid, or else

the statute itself is unconstitutional. The situation is comparable to that in *Counselman v. Hitchcock*, 142 U. S. 547, 35 L. Ed. 1110, wherein the immunity provisions of the Fifth Amendment were sought to be met by provisions granting to those who testified immunity from prosecution. Because the statute was not as broad as the constitutional guaranty, the Supreme Court held the statute unconstitutional.

II.

The attempted delegation of authority to the investigator of the Securities and Exchange Commission to subpoena at his whim any books and records would constitute a roving commission. It would indeed be delegation running riot. Congress never intended such a wide authority and did not grant it. It would enable any investigator to do that which only the Commission itself has a right to decide might be done.

As to delegation running riot, the investigator would be in the same position as those condemned in the earlier decisions of England and America. (See *Boyd v. United States*, 116 U. S. 616.)

III.

The attempt to delegate the absolute power to make a finding as to what should be subpoenaed is itself a violation of Article III of the Constitution of the United States granting judicial powers only to the judiciary. The Fourth Amendment to the Constitution forbids against unreasonable searches and seizures. The judiciary is given the power to pass on whether the search is or is not unreasonable. Can Congress confer this power upon the Securities

and Exchange Commission and require that the Commission itself make an absolute finding as to whether its investigation, the books, papers and records which it is seeking to investigate, are relevant and material to its inquiry which would be absolutely binding on the courts? We contend that this is a judicial function and that in so far as the statute attempts to give this power to the Securities and Exchange Commission it is unconstitutional as a violation of Article III of the Constitution of the United States.

IV.

The Contract Was Not Within the Jurisdiction of the S. E. C.

The bottling contract in this case was as follows:

"Federal Alcohol Administration Wholesaler's Basic Permit No. PD-12377

The Penfield Company of California

Distillery Factors and Controllers

Spring Arcade Building

Los Angeles, California

No..... Dated.....

Name..... Address

Hereinafter called the seller and The Penfield Company of California, hereinafter called the buyer, contract and agree between themselves unto the following:

1. In consideration of the execution of the within sales agreement, the seller hereby sells and assigns to the buyer, the following described whiskey:

.....

Distillery Barrels Serial Nos. When Made Tax Due

.....

Now Insured With.....

Storage or Other Charges Paid to.....

Title to said whiskey to pass to the buyer from the seller upon delivery of warehouse receipts, as described above, and the execution of this agreement.

2. The buyer intends to cause the said whiskey to be bottled after the same has reached four years of age or over, and intends to offer or cause to be offered such bottled goods for sale. After said whiskey has been bottled and sold, the buyer shall pay to the seller such an amount which the buyer received from the sale of said bottled goods, less all insurance, storage, taxes, costs, expenses advanced or incurred by the buyer, transportation, bottling, stamping, labeling, and ten per cent of the gross per case sales price. The buyer shall furnish to the seller figures compiled from government records showing the actual amount of whiskey in barrels and number of vases it produced, together with prices received. The buyer reserves the right to bottle and pay for any portion of said whiskey from time to time as contemplated herein.

3. The seller vouches himself to be the true and lawful owner of the within warehouse receipts with full right and authority to dispose of the same in the manner aforesaid, and further agrees that the buyer may do any and all things which in the buyers opinion are incident to the interests herein, and the seller further agrees to warrant and defend the said warehouse

receipts to the said buyer against all claims and demands.

4. This contract contains the entire agreement of the parties hereto, and the seller agrees that no representations were made other than those herein set forth.

5. This contract executed in duplicate, is subject to acceptance by the buyer at its office. An exact copy of this agreement is hereby acknowledged which is an interim receipt for the above whiskey, pending receipt of the executed original agreement.

Witness..... .....Seller
(Seal)

Accepted

THE PENFIELD COMPANY OF CALIFORNIA

By .....
President-Treasurer Buyer

(The distilled spirits herein will be packaged before sale in bottles labeled and marked in accordance with law and the rules and regulations of the Federal Alcohol Administration.)"

This contract did not constitute an investment contract.

In its generic sense of the word every contract is an "investment contract" but in these proceedings contracts which merely deal with the recipients making a profit from the bottling of whiskey is not the type of contract which gives the Securities and Exchange Commission jurisdiction.

People v. Davenport, 21 Cal. App. (2d) 252

A security does not extend to ordinary commercial contracts, nor does it include interest income from the lending of money or the profits which one might make from his own efforts as the result of any ordinary commercial contract. (*Lewis v. Creasey Corp.*, 198 Ky. 407, 248 S. W. 1046.)

V.

The District Court Erred Therefore in Holding That Bottling Contracts of The Penfield Company of California Were Transactions in Securities as Defined in Section 2(1) of the Securities Act of 1933 and Therefore Conferred Jurisdiction Upon the Securities and Exchange Commission.

These contracts were contracts to bottle whiskey and pay the tax on it. They were not contracts for a security, but for the performance of certain work and labor in connection with the bottling of whiskey. Many wholesalers, retailers, large corporations, hotels, etc., daily send warehouse receipts owned by them to licensed bottlers with instructions to the bottlers to "tax pay" the whiskey, bottle and label it and ship it to them through the regular channels of bottler to a licensed wholesaler, wholesaler to licensed retailer, retailer to the original owner, etc., as the case may require. The bottler bills the wholesaler for the taxes and other charges he has paid, plus his cost of bottling. The wholesaler bills the retailer for the same charges, plus his handling fee, and the retailer does likewise.

There is nothing in the transaction, therefore, that makes it a security within the meaning of the Securities Act.

VI.

The District Court Erred in Holding That Transactions in Distillers' Whiskey Warehouse Receipts and Matters Relating to Alcohol Were Transactions Within the Meaning of Section 2(1) of the Securities Act as Amended in 1933.

A warehouse receipt represents the property described therein, and a transfer of the same is a symbolic delivery of the goods called for by the receipt and passes title to the goods as effectually as if an actual delivery were made. (Civ. Code, sec. 1858b; *A. Widemann Co. v. Digges,* 21 Cal. App. 342, 131 Pac. 882; *Cavallaro v. Texas etc. Ry. Co.,* 110 Cal. 348, 42 Pac. 918, 52 Am. St. Rep. 94; *Garoutte v. Williamson,* 108 Cal. 135, 41 Pac. 35; *Bishop v. Fulkerth,* 68 Cal. 607, 10 Pac. 122; *Davis v. Russell,* 52 Cal. 611, 28 Am. Rep. 647.) Thus, by the issuance or transfer of a warehouse receipt for whiskey held in bond in Kentucky, there is in fact a sale and a constructive delivery within the state of California of a commodity, although at the time of the sale it is and may forever remain elsewhere, and as between the vendor and the vendee there is no distinction between the solicitation of orders for the whiskey and the solicitation of orders for warehouse receipts representing the same.

VII.

The District Court Erred in Holding That Each of the Twenty Items Was Within the Scope and Jurisdiction of the Securities Act Giving the Commission Power to Investigate Them.

The District Court erred in holding that each of the twenty items which the subpoena, issued by an employee of the Securities and Exchange Commission, sought to get, was within the scope and jurisdiction of the Securities Act, giving the Commission power to investigate them.

It was error for the District Court to grant the application of the Commission and to issue its order requiring appellant to produce for examination by the Commission or its representatives "All books, records, documents, contracts, agreements, checks, bank statement, correspondence files and all other papers and memoranda in which have been entered a record of the transactions and business of The Penfield Company of California *from the date of its incorporation to the date of this subpoena*, including in particular, the following:" followed by items numbered 1 to 20, inclusive, of said Order.

The record shows that many of these things were not within the scope or sphere of the Securities and Exchange Act. The taking of them constituted an unreasonable search and seizure. (*Jones v. Securities and Exchange Commission*, 298 U. S. 1, 80 L. Ed. 1015; *Hale v. Henkel*, 201 U. S. 43, 55 L. Ed. 873; *Federal Trade Commission v. American Tobacco Co.*, 264 U. S. 298; *Boyd v. United States*, 116 U. S. 616, 29 L. Ed. 746; *Interstate Com. Commission v. Brimson*, 154 U. S. 447.)

The measure of power is the mode prescribed in the statute.

Stark v. Wickard, 88 L. Ed. 511, 522;
Head v. Providence Insurance Co., 2 Cranch. 156;
Zottman v. S. F., 20 Cal. 102;
Michelson v. Painter, 35 Cal. 705;
People v. Gunn, 85 Cal. 238, 248.

In *Annenberg v. Roberts,* 333 Pa. 214, decided by the Supreme Court of that state (1938), the court after quoting the above excerpt from the opinion of Chief Justice Rugg of the Massachusetts Supreme Court added (p. 214):

> "While the act under consideration in the present case seems to recognize this fundamental principle, since it authorizes the issue only of such subpoenas as require answers to questions *'touching matters properly being inquired into by the Commission'* and the compulsory production only of such books, papers, records and documents as relate *'to the subject of inquiry,'* we are in accord with the observations made by the court below as to the irrelevance of information called for in the subpoenas issued to these plaintiffs; it follows that there is a constitutional lack of power in the Commission to demand it." (Italics supplied.)
>
> "The subpoenas show on their face that they contemplate an unreasonable search and seizure. They violate the principle which we announced in *American Car & Foundry Co. v. Alexandria Water Co.,* 221 Pa. 529, where we held that a subpoena *duces tecum* could not properly be issued to bring in a mass of books and papers in order that there might be a search through them to gather evidence. We, therefore, are of opinion that the subpoenas as issued

commanding plaintiffs to produce before the Commission the things therein set forth are void, in that they do not show that the demands are germane to the inquiry authorized by the Governor's call. . . ."

VIII.

The District Court Erred in Holding That the Provisions of Section 19(b) of the Securities Act of 1933 as Amended and Supplemented by the Provisions of Section 22(b) of Said Act, Inherently and as Construed and Applied in This Case, Are Not Invalid and Unconstitutional Because They Delegate Judicial Powers to the Securities and Exchange Commission in Violation of Article III of the Constitution of the United States, and Deprive the District Court of Judicial Functions as to What Matters Are or Are Not Relevant or Material to the Inquiry.

Pacific Railway Commission v. Stanford, 32 Fed. Rep. 241, approved in *Interstate Commerce Com. v. Brimson,* 154 U. S. 447, and *Innes v. Securities and Exchange Commission,* 80 L. Ed. 1015.

The power of the S. E. C. to make findings as to whether books, papers, or documents are material to the inquiry, binding upon the courts is here challenged, since that body does not have judicial powers. The act therefore unconstitutionally delegates these powers to the Commission.

For all of which reasons petitioners pray that a writ of certiorari be granted and that the judgment and order below be reversed.

Respectfully submitted,

MORRIS LAVINE,
Attorney for Appellant.

State of California, County of Los Angeles—ss.

Morris Lavine, being first duly sworn, upon his oath deposes and says that he is one of the counsel for the appellants, The Penfield Company of California, Appellant; that he has read the foregoing Petition for Writ of Certiorari to the Ninth Circuit Court of Appeals of the United States and Brief in Support Thereof, and knows well the contents thereof; that he has carefully read and studied the transcript of record and proceedings in the case at bar; that the matters in said petition are in the judgment of this affiant duly supported in and by said transcript of record and proceedings, and that he verily believes the facts stated in said petition are true.

MORRIS LAVINE.

Subscribed and sworn to before me this 14th day of September, 1944.

ZOA L. ZACCHE,

Notary Public in and for said County and State.

Office - Supreme Court, U. S.
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CLERK

No. 475

In the Supreme Court of the United States

October Term, 1944

THE PEOPLE OF [illegible]

v.

[illegible]

ON [illegible]

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In the Supreme Court of the United States

OCTOBER TERM, 1944

No. 475

THE PENFIELD COMPANY OF CALIFORNIA, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

OPINION BELOW

The opinion of the circuit court of appeals (R. 345) has not yet been officially reported. The district court rendered no opinion.

JURISDICTION

The judgment of the circuit court of appeals was entered on June 30, 1944 (R. 360–361), and rehearing was denied on August 8, 1944 (R. 361). The petition for a writ of certiorari was filed on September 16, 1944. The jurisdiction of this Court is invoked under Section 240 (a) of the

Judicial Code, as amended by the Act of February 13, 1925, which is made applicable by Section 22 (a) of the Securities Act of 1933.

QUESTION PRESENTED

Whether the court below properly affirmed a district court order enforcing a subpoena *duces tecum* issued by officers of the Securities and Exchange Commission in connection with an investigation into suspected violations of the Securities Act of 1933.

STATUTE INVOLVED

The applicable provisions of the Securities Act of 1933 (15 U. S. C. 77a *et seq.*) are set forth in the Appendix, *infra,* pp. 10–12.

STATEMENT

Pursuant to Section 20 (a) of the Securities Act (15 U. S. C. 77t (a)), the Commission is conducting an investigation to determine whether petitioner and other specified persons have violated Sections 5 (a) and 17 (a) (15 U. S. C. 77e (a) and 77q (a)) by selling petitioner's stock and securities consisting of whiskey-bottling contracts without registration and by means of untrue statements of material facts (R. 8–15). The investigation was instituted by order of the Commission upon information tending to establish certain facts, recited in the order, which indicated that petitioner and others had violated the Act (R. 8–15). In this order (and in a subsequent supplemental order) the Commission empowered cer-

tain of its officers "to administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of any books, papers, correspondence, memoranda or other records deemed relevant or material to the inquiry" (R. 11, 15). Accordingly, one of the designated officers directed a subpoena to petitioner requiring it to produce certain of its books, papers, and documents which are specifically itemized (R. 15–18).

Petitioner failed to comply with the subpoena and the Commission applied to the district court for its enforcement (R. 2–19) pursuant to Section 22 (b) of the Act (15 U. S. C. 77v (b)). The Commission showed that purchasers of whiskey warehouse receipts from petitioner or from another company under investigation, Bourbon Sales Corporation, had been induced to turn over the receipts to petitioner in exchange for bottling contracts or stock; that the bottling contracts had been offered or sold through the mails on the representation that the only way the receipt holders could earn a profit would be by utilizing the facilities of Bourbon Sales Corporation or petitioner enabling those companies to bottle and sell the investor's whiskey with minimum expense and at the highest price; and that petitioner's stock had been sold through the mails by means of literature which omitted to state its true book value and contained misrepresentations concerning petitioner's profit potentialties (R. 160, 162, 190–193, 201–204, 340, 342).

The district court granted the Commission's application, specifically ordering the petitioner to produce all the items, twenty in number, which were enumerated in the subpoena (R. 311, 313–316). The circuit court of appeals affirmed (R. 344).

ARGUMENT

1. Presumably on the theory that certain of the items in the subpoena related only to the whiskey bottling contracts and not to the sale of its stock, petitioner asserts that there is error in the determination that these contracts are securities within the meaning of Section 2 (1) of the Act (15 U. S. C. 77b (1)).[1]

This determination by the circuit court of appeals (not by the district court, as stated by petitioner (Br. 19)), was not necessary to the decision. Examination of the face of an instrument is not always sufficient to determine whether it is a security within the meaning of Section 2 (1) of the Act. The "plan of distribution, and the economic inducements held out to the prospect" are material considerations in such a determination. *Securities and Exchange Commission* v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344, 353. The Commission could properly inquire into the circumstances of the issuance and sale of

[1] Petitioner argues also that the district court erred in holding that the warehouse receipts (as distinguished from the bottling contracts) were securities (Br. 20). No such holding was made by either court below and the Commission has expressed no opinion as to whether the whiskey warehouse receipts, standing alone, are securities.

the bottling contracts in order to elicit facts indicating whether they constituted securities within the purview of the Act. The Commission is entitled to the enforcement of any subpoena which is "not plainly incompetent or irrelevant to any lawful purpose" in the discharge of its duties under the Act. *Endicott-Johnson Corporation* v. *Perkins,* 317 U. S. 501, 508–509. In the light of the *Joiner* case, *supra,* it is clear that the subpeona complied with this standard.

Moreover, the determination of the court below that the bottling contracts are securities is correct. Persons who had previously purchased whiskey warehouse receipts were offered and sold these contracts upon the representations that petitioner or Bourbon Sales Corporation would take care of all details in taking the whiskey out of bond, bottling it and selling it, and would see that the investor received a profit (R. 86, 88–89, 160, 162, 190–193, 201–204, 340, 342). The contract holders were to do nothing; indeed, they did not have the facilities or the necessary federal and state liquor licenses (R. 96, 166) to take the whiskey out of bond and dispose of it. Petitioner represented that there would be a pooling of the whiskey it purchased from various receipt holders (R. 159–160) so that, under the scheme, each contract holder would get no more than a right to share in the avails of a mass of whiskey processed by petitioner. Under these circumstances, the bottling contracts fall within the

statutory definition of Section 2 (1), which specifically includes as a "security" any "certificate of interest or participation in any profit-sharing agreement," any "investment contract," and "any interest or instrument commonly known as a 'security.'" The record makes clear that the entire scheme involved, in substance, a speculative investment in a common enterprise necessarily contemplating complete reliance by the investor upon the efforts of the seller. The bottling contracts were given the character of securities by "the terms of the offer, the plan of distribution, and the economic inducements held out to the prospect." *Securities and Exchange Commission* v. *C. M. Joiner Leasing Corp.*, 320 U. S. 344, 352–53.

2. Petitioner urges that under Section 19 (b) only those books, papers and documents which the Commission itself has found relevant or material to the inquiry may be subpoenaed, and that no such finding was made in this case. It should first be noted that when the Commission authorized these enforcement proceedings to be taken, it did pass on the relevancy and materiality of the documents sought (R. 5). Thus, petitioner ultimately received the benefit of the Commission's judgment to which it contends it is entitled.

In any event, the court below properly held that under Section 19 (b) the determination as to what books, papers, or other documents are relevant

and material to the inquiry may be delegated to the officers designated by the Commission to conduct the investigation. *Woolley* v. *United States,* 97 F. (2d) 258, 262 (C. C. A. 9), certiorari denied, 305 U. S. 614. See also H. Rep. No. 85, 73d Cong., 1st sess., p. 25. The Commission itself, of course, formally decides that the facts in its possession warrant an inquiry to determine whether the Act has been violated. And the statutory provision authorizing the Commission to delegate its subpoena powers, which was recognized by this Court in *Cudahy Packing Co.* v. *Holland,* 315 U. S. 357, 365, would be eviscerated were the officers to whom the power was delegated nevertheless required thereafter to return to the Commission for a decision as to the relevancy and materiality of the documents to be subpoenaed. There is no warrant for saying that the delegation authorized by Section 19 (b) is merely the delegation of the purely ministerial and mechanical functions involved in the issuance of a subpoena. To so hold would be inconsistent with the provision relating to the appointment of examining officers and would seriously hamper effective administration. The delay which would necessarily result from such an interpretation of Section 19 (b) would be particularly injurious in view of the three-year period of limitation (Act of December 27, 1927, 45 Stat. 51, 18 U. S. C. 582) on criminal prosecutions under the Securities Act (Sec. 24; 15 U. S. C. 77x).

3. Petitioner asserts finally that the order enforcing the subpoena authorizes an unlawful seizure contrary to the Fourth Amendment, and that the provision of Section 19 (b) of the Act giving the Commission power to issue a subpoena *duces tecum* is a delegation of judicial power in violation of Article III of the Constitution.

The short answer to this latter argument is to be found in its rejection by this Court, fifty years ago, in *Interstate Commerce Commission* v. *Brimson,* 154 U. S. 447, 476.

As to the "search and seizure" argument, the Fourth Amendment requires only that the demand be reasonably specific and limited to documents relevant to the inquiry. *Wilson* v. *United States,* 221 U. S. 361, 375–376; *Baltimore & Ohio Railroad Co.* v. *Interstate Commerce Commission,* 221 U. S. 612, 622; *McMann* v. *Securities and Exchange Commission,* 87 F. (2d) 377, 379 (C. C. A. 2), certiorari denied, 301 U. S. 684. Although petitioner speaks of "an arbitrary finding" as to what is relevant and material, it has not attempted to show that any of the twenty items specified in the subpoena is irrelevant or immaterial to the inquiry.[2] Consideration of these items (R. 15–18)

[2] In fact, the only specific criticism which petitioner makes on this score is directed to language which appeared only in the order to show cause (R. 20) and is not found in either the subpoena or the order under review (R. 15–18, 313–316). This language in the order to show cause referred to "All

in the light of the subject of the Commission's inquiry shows that the court below correctly found that "The twenty items of the subpoena are within the normal area of such an investigation" (R. 357).

CONCLUSION

The decision below is correct, and there is no conflict of decisions. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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MILTON V. FREEMAN,
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OCTOBER 1944.

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books, records, documents, contracts, agreements, checks, bank statement, correspondence files and all other papers and memoranda in which have been entered a record of the transactions and business of The Penfield Company of California * * * "from the date of its incorporation to the date of this subpoena" (Br., 21).

APPENDIX

The pertinent sections of the Securities Act of 1933 (48 Stat. 74, as amended by the Act of June 6, 1934, 48 Stat. 905, 15 U. S. C. 77a *et seq.*) are as follows:

SECTION 2. When used in this title, unless the context otherwise requires—

(1) The term "security" means any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, or, in general, any interest or instrument commonly known as a "security," or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

* * * * *

SECTION 5 (a). Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—

(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell or offer to buy such security through the use or medium of any prospectus or otherwise; or

(2) to carry or cause to be carried through the mails or in interstate commerce,

by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.

SECTION 17 (a). It shall be unlawful for any person in the sale of any securities by the use of any means or instruments of transportation or communication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

SECTION 19 (b). For the purpose of all investigations which, in the opinion of the Commission, are necessary and proper for the enforcement of this title, any member of the Commission or any officer or officers designated by it are empowered to administer oaths and affirmations, subpena witnesses, take evidence, and require the production of any books, papers, or other documents which the Commission deems relevant or material to the inquiry. Such attendance of witnesses and the production of such documentary evidence may be required from any place in the United States or any Territory at any designated place of hearing.

SECTION 20 (a). Whenever it shall appear to the Commission, either upon complaint or otherwise, that the provisions of

this title, or of any rule or regulation prescribed under authority thereof, have been or are about to be violated, it may, in its discretion, either require or permit such person to file with it a statement in writing, under oath, or otherwise, as to all the facts and circumstances concerning the subject matter which it believes to be in the public interest to investigate, and may investigate such facts.

SECTION 22 (b). In case of contumacy or refusal to obey a subpena issued to any person, any of the said United States courts, within the jurisdiction of which said person guilty of contumacy or refusal to obey is found or resides, upon application by the Commission may issue to such person an order requiring such person to appear before the Commission, or one of its examiners designated by it, there to produce documentary evidence if so ordered, or there to give evidence touching the matter in question; and any failure to obey such order of the court may be punished by said court as a contempt thereof.

SECTION 24. Any person who willfully violates any of the provisions of this title, or the rules and regulations promulgated by the Commission under authority thereof, or any person who willfully, in a registration statement filed under this title, makes any untrue statement of a material fact or omits to state any material fact required to be stated therein or necessary to make the statements therein not misleading, shall upon conviction be fined not more than $5,000 or imprisoned not more than five years, or both.

U. S. GOVERNMENT PRINTING OFFICE: 1943